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In the Supreme Court of the United States

OCTOBER TERM, 1973

No. 73-38

UNITED STATES OF AMERICA, APPELLANT

v.

MARINE BANCORPORATION, INC., NATIONAL BANK OF COMMERCE OF SEATTLE, WASHINGTON TRUST BANK, AND JAMES E. SMITH, COMPTROLLER OF THE CURRENCY

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF WASHINGTON

BRIEF FOR THE UNITED STATES IN OPPOSITION TO MOTIONS TO AFFIRM

1. The government contends that National Bank of Commerce ("NBC") was a potential entrant into the Spokane market because, *inter alia,* it could have sponsored a new national bank there as an affiliate and later acquired it. The appellee banks argue that NBC could not in fact have done so because such conduct would violate provisions in Washington law limiting branch banking, and that NBC would not have done so because the settled practice among Washington banks has been to the contrary.

The record shows, however, that Washington banks have for many years gained entry into areas in which they could not establish *de novo* branches by sponsoring new banks in those areas and subsequently acquiring them.[1] The federal regulatory authorities, including appellee Comptroller, are aware of this practice and have never objected to it when considering specific applications by national banks in Washington.[2] The merging banks NBC [3] and WTB [4] have also been aware of the sponsorship activities of other Washington banks.

Indeed, officers of NBC themselves considered sponsoring an affiliate in several instances.[5] Moreover, NBC sponsored a new bank in South Central Washington, the Columbia Center National Bank, for the purpose of acquiring it in the future.[6] It has never been suggested that either these sponsorship activities by NBC and its officers, or the practice itself is illegal.[7]

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[1] See Tr. 280–298, GX H–1 and H–11.

[2] GX H–1, H–3, H–4, H–5, H–6, H–7, H–8, H–11, H–12, H–13 and H–14 show that all three federal bank regulatory agencies are aware of the practice among major Washington banks of sponsoring new banks in furtherance of their expansion programs.

[3] GX I–4b, I–6b, I–7, I–8a, I–8b, I–9a, I–9b, I–10a, I–10b, I–11a, I–11b, I–11c, I–11d, J–45, J–46.

[4] GX C.

[5] GX I–3, I–4c, I–4d, I–4e, I–5.

[6] GX J–1 through J–54; GX K–1 through K–94.

[7] During the trial, the district court flatly rejected appellees' assertion that NBC could not legally sponsor the formation of a new national bank as a vehicle for its entry into Spokane (Tr. 732–733):

"I don't conclude * * * that there is anything wrong with that approach. * * * [T]he only thing is, they had the capa-

Contrary to appellees' contention, *First National Bank* v. *Walker Bank*, 385 U.S. 252, does not indicate that such sponsorship by NBC would be prohibited under the National Bank Act. That case held that the provision of that Act governing branch banking (12 U.S.C. 36(c)) permits national banks to establish branches only in accordance with state law. The establishment of a new national bank, however, even where sponsored by an existing bank, is governed by other provisions of the Act (12 U.S.C. 26, 27) which do not require compliance with state law restrictions on branch banking. This distinction between the chartering of new, bona fide national banks to be affiliated with existing banks, and branching by existing banks, is reflected in the decisions of other federal courts;[8] in the Comptroller's decisions cited above (n. 2, *supra*, p. 2), and in the subsequent history of the *Walker Bank* case itself.

In *Walker Bank* this Court held that it was unlawful for The First National Bank of Logan to establish a *de*

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bility, and they had done it, if that is what you are trying to prove.

* * * * *

"Well, I have no doubt about that, I had no doubt about that right from the beginning of the case. I think they can go in. They can help organize one, they can loan money, and all the rest of it, and they could probably do it in Spokane. I will agree that they could do that."

[8] *Ramapo Bank* v. *Camp*, 425 F.2d 333 (C.A. 3), certiorari denied, 400 U.S. 828; *Camden Trust Co.* v. *Gidney*, 301 F.2d 521 (C.A.D.C.), certiorari denied, 369 U.S. 886; *Pineland State Bank* v. *Proposed First National Bank of Bricktown*, 335 F. Supp. 1376 (D. N.J.); *Traverse City State Bank* v. *Empire National Bank*, 228 F. Supp. 984 (W.D. Mich.).

novo branch in Logan. The Comptroller then authorized the establishment of a new national bank (Pioneer National Bank), sponsored by persons associated with First National Bank of Logan. Subsequently, the Comptroller approved the merger of Pioneer National Bank into First National Bank of Logan, so that the latter in effect obtained the Logan office it originally sought.[9]

Since the chartering of national bank affiliates is not governed by state law, it is apparent that the provisions of Washington law barring a newly-chartered state bank from being acquired for ten years without the consent of the State Supervisor of Banking are also inapplicable.

Appellee banks (Motion, p. 21, n. 15) characterize the practice of Old National Bank of Washington, a subsidiary of Washington Bancshares, Inc., of sponsoring and later acquiring new national banks in areas

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[9] Decision of the Office of the Comptroller of the Currency on the Application to Merge Pioneer National Bank, Logan, Utah, with The First National Bank of Logan, Logan, Utah, April 23, 1973. As the Comptroller explained in his opinion (p. 1):

"Pioneer National Bank, the merging bank, was chartered in January 1968 by persons associated with The First National Bank of Logan after an attempt by that bank to establish a branch in Logan was stifled on legal grounds [*i.e.*, this Court's decision in the *Walker Bank* case, *supra*]. Pioneer National Bank has operated as an affiliate of the charter bank since its inception and these two banks have a common directorate as well as common stock ownership; * * *."

See also, Advisory Report of the Board of Governors of the Federal Reserve System on the Competitive Factors Involved in the Proposed Merger of Pioneer National Bank and First National Bank of Logan, March 22, 1973, p. 1: "Due to Court action, the branch was closed on January 26, 1968, and a few days later Pioneer was established at that location."

where it could not establish *de novo* branches, as a "violation of both state and federal law." Although they assert that the Comptroller would not have granted the charters for the national banks had he known that the plan was to obtain branches for Old National Bank, the record shows that the Comptroller was fully informed of the sponsoring banks' intention prior to the filing of the applications [10] (Tr. 288–289). Indeed, in one instance, officials of the Comptroller's Office actually suggested this procedure (*ibid.*).[11]

Finally, appellee banks suggest (Motion, p. 20) that sponsorship of a new bank by NBC might result in the forfeiture of the charter of its parent, Marine Bancorporation, under a provision of Washington law [12] which prohibits a bank holding company from owning or controlling more than 25 percent of the stock of another bank. The statute, however, only bars such

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[10] There was one exception: the Comptroller was not informed of Old National Bank's intention to acquire a state bank it had assisted in forming until after that bank had been formed (Tr. 288).

[11] The Comptroller's approval of sponsorship and acquisition as a method of achieving *de novo* entry undermines the testimony by the Regional Administrator of National Banks, upon which appellee banks rely (Motion, p. 19), that his office would not approve a charter application where the applicants disclosed a purpose of establishing the newly created bank as a branch of an existing bank. In any event, that testimony came in response to a question which assumed that the applicants disclosed that the "*sole* purpose" of the application was to establish a branch (Tr. 975). This response, therefore, has no bearing on the situation where the sponsored affiliate operates as a *bona fide* national bank for a period of time before its sponsor acquires it, as did the sponsored affiliates of Old National Bank.

[12] RCW 30.04.230.

ownership or control by a bank holding company, and does not cover ownership or control merely by persons affiliated with a holding company or one of its operating subsidiaries. This provision has not prevented Old National Bank of Washington and its parent Washington Bancshares, Inc., or NBC itself from sponsoring affiliates (see nn. 1 and 6, *supra*, p. 2.).[13]

2. Appellees contend that the district court properly approved the merger on the alternative ground that, even assuming that the government had established the anticompetitive effects alleged in the complaint, those effects were clearly outweighed by the benefits the merger would provide in serving the convenience and needs of the community. The Bank Merger Act, however, does not permit a district court to apply the convenience and needs standards on the basis of a hypothetical assumption with respect to the charged violation of Section 7 of the Clayton Act. Before a merger with anticompetitive effects may be approved under the "convenience and needs" defense, the court is required to balance the actual anticompetitive effects against the community convenience and needs that the merger would serve, and it may approve the merger only if the latter factors clearly outweigh the anticompetitive effects. See our Jurisdictional

[13] Appellees point out (Bank's Motion to Affirm, p. 27, n. 17; Comptroller's Motion to Affirm, p. 17, n. 10) that the Jurisdictional Statement cites certain documents that were not admitted into evidence. With respect to some of them, other documents in evidence support the propositions for which the excluded documents were cited. In the case of two depositions, government trial counsel believes that they were admitted in evidence but that the court reporter's transcript erroneously fails to show that fact. These documents are discussed in the appendix, *infra*.

Statement, p. 23. If, as we contend, this merger does have the anticompetitive effects condemned by Section 7, the district court must conduct the balancing on the basis of the actual facts relating to the anticompetitive effect, not a hypothetical case.

In any event, the record here shows that the anticompetitive effects of this merger were not "clearly outweighed in the public interest" by the benefits in serving the community convenience and needs which the district court found. The benefits that the district court cited were primarily the additional services that the merger will enable Washington Trust to perform in Spokane. Although all these services are currently available from other banks there (Tr. 949), appellees contend, and the district court held, that the community would benefit from an alternate source for these services. The additional services include an increase in Washington Trust's lending limit from $1.25 million to $7.5 million; international banking services; mining, agricultural, and student loans; and municipal bond financing. The district court concluded that increased competition for these few specialized banking services would increase economic growth in Spokane to the benefit of all banking customers (J.S. App., p. 46).

The convenience and needs defense, however, requires a showing that the services offered by the new bank are "likely to benefit *all* seekers of banking services in the community * * *." *United States* v. *Phillipsburg Nat. Bank,* 399 U.S. 350, 372 (emphasis added). Appellees have not made that showing. The additional services that the merger would enable

Washington Trust to provide would benefit only a small number of banking customers. Appellees have not shown that there is a substantial unsatisfied demand for mining, agricultural and student loans. The number of customers seeking loans up to $7,500,000 necessarily is small. Similarly, the greater availability of municipal bond financing can benefit only a few borrowers. Moreover, these latter two services ordinarily are provided by banks that operate in national or regional rather than local markets.

3. The merger will have serious adverse effects outside the Spokane area, which may substantially lessen competition in the Eastern Region of Washington and in the State of Washington as a whole. These areas are not banking markets, *i.e.*, areas within which most customers may conveniently find sellers of banking services. See *United States* v. *Philadelphia Nat. Bank*, 374 U.S. 321, 357–359. They are, however, "section[s] of the country," economically differentiated from other areas, within which the merger may "substantially lessen competition." Since the purpose of defining a "section of the country" under Section 7 is to focus upon the geographic area where the merger will have a significant impact upon competition (*United States* v. *Pabst Brewing Co.*, 384 U.S. 546, 549–550), it is necessary to consider the effect of this merger in those broader areas.

a. State boundaries delineate a distinct area within which banks are legally insulated from competition by

banking institutions located outside the state.[14] Banks in the state are required to confine their market extensions (*i.e.*, the establishment or acquisition of banking offices in local banking markets where they have not previously competed) within the state boundaries. If, as a result of mergers and acquisitions, the same few large institutions face each other in most of the state's major local banking markets, then competition in the state, as a "section of the country" greater than the banking markets within it, may be substantially lessened.

Oligopolistic behavior in local banking markets will not be limited by the threat of potential *de novo* or foothold entry by other banks, since the significant potential competitors in the state, *i.e.*, the major banks in local markets capable of expansion elsewhere, will have been eliminated by merger. Thus in this case the acquired bank is being eliminated as a potential entrant into other local markets in Eastern Washington. Moreover, once the same few banking institutions have purchased large market shares in most of a state's local banking markets, the local oligopolies in each such market become linked. As a result, the statewide institutions may engage in more standardized, and hence less competitive business behavior everywhere,

[14] Very large banking customers, such as national corporations, and very large banks, however, can be said to operate in regional and national banking markets irrespective of state boundaries, since convenience of access is not a limiting factor at this level. For the vast bulk of banking customers, however, convenience is the key element in defining banking markets. See *United States* v. *Philadelphia Nat. Bank*, *supra; United States* v. *Phillipsburg Nat. Bank*, *supra.*

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rather than risk retaliation by competing locally anywhere.[15]

In contrast, if the expansive drive of the state's large banks is channeled into entry into local markets by *de novo* or foothold acquisitions, then they will have to compete vigorously to enlarge their initial small market shares. They will thus bring to local markets throughout the state a new competitive force, which can challenge the entrenched positions of the locally dominant banks.[16] This is the competition the merger will eliminate.

b. NBC, the acquiring bank, is the second largest bank in Washington, where commercial banking is already highly concentrated. The five largest banks have approximately three-fourths of total deposits in the state. Banking concentration is even higher in Eastern Washington, an economically distinct region in the state; the five largest banks operating there hold 84 percent of the area's total deposits (J.S., pp. 4–5). Moreover, the five largest banks in the state in varying combinations hold a dominant share of deposits in practically all the local banking markets in the state (GX A–35).

[15] See, Solomon, *Bank Merger Policy and Problems: A Linkage Theory of Oligopoly*, 89 The Banking Law Journal 116, 119 (1972).

[16] Cases under Section 2 of the Sherman Act have recognized that even though a particular firm operates in local markets, the relevant section of the country may be broader. *United States* v. *Grinnell Corp.*, 384 U.S. 563; *Otter Tail Power Co.* v. *United States*, 410 U.S. 366; *United States* v. *Griffith*, 334 U.S. 100, *Schine Theatres* v. *United States*, 334 U.S. 110. The same considerations apply to determining the "section[s] of the country" within which anticompetitive probabilities are assessed under Section 7 of the Clayton Act. *United States* v. *Pabst Brewing Co.*, 384 U.S. 546, 549–550.

Washington Trust, the acquired bank, is the eighth largest bank in the state, the third largest in Spokane, and is a growing institution ready to expand beyond Spokane (J.S., p. 6). With assets of $112 million, it is one of only 12 middle-sized banks in Washington (*i.e.*, banks with assets in the $250 million to $30 million range) (GX A–2) capable of expanding into other local markets.

As developed in our Jurisdictional Statement, we believe that this merger may substantially lessen competition in the Spokane market by eliminating NBC, the acquiring bank, as a potential competitor (both actual and perceived) in that market. But the anti-competitive effects of this merger must also be evaluated in the broader context of the prevailing banking structure in Eastern Washington and in the state as a whole.

Washington Trust (the acquired bank) is one of a few banks which has the potential for entering new markets in Eastern and other sections of Washington. Moreover, its acquisition by one of the state's dominant banks will add Spokane to the number of local banking markets in which the few large banks in the state face each other as dominant factors, thus contributing to the creation of a statewide banking structure of commonly linked local oligopolies. This creates a real danger that the large banks will renounce vigorous competition,[17] and instead pursue parallel practices of mutual advantage without regard to local competitive conditions.

[17] The large banks in Washington have shown a tendency to pursue parallel, and in some instances cooperative, behavior (see GX B–1, B–2, B–3, F–29, F–31, Dep. R. Buck, pp. 53–57).

By disregarding the regional and statewide implications of the acquisition, therefore, the district court severely, and erroneously, limited its assessment of the merger's probable competitive effects.

Respectfully submitted.

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OCTOBER 1973.

APPENDIX

Documents cited in the government's Jurisdictional Statement that were not admitted in evidence.

1. *GX F–21, F–24, F–28 and F–29.* They were cited (J.S., p. 19) to support the government's contention that NBC had made known its interest in entering the Spokane market. This proposition is supported by GX F–23, F–25, F–26 and F–31, all of which were admitted. Moreover, GX F–21 was admitted as an exhibit to the Carlson Deposition, received in evidence at Tr. 327. When GX F–21 was offered to show NBC's interest in acquiring Washington Trust and the services of one of its officers, however, it was rejected as immaterial (Tr. 595). GX F–24, GX F–28 are each the second page of a two-page document, the first page of which was admitted and the second page of which was not.

2. *GX F–3, F–10, F–11 and F–19.* They were cited (J.S., p. 18, n. 11) to show that the Comptroller favored the merger prior to considering the application for its approval. These exhibits were offered but rejected by the district court (Tr. 582, 1020) as immaterial. The district court stated (Tr. 1006), however, "* * * I'll take it as being the fact that [NBC] talked with the Comptroller and the chief deputy and the chief deputy or Comptroller, whoever it was, said * * * that he would look with favor on it if the application were made, that's all. I'll accept it as being the fact—that's what he said." The court therefore recognized that the Comptroller favored the merger.

3. *GX F–14* was cited (J.S., p. 6) to support the proposition that the acquired bank's officers were paid rates

comparable to those paid by the state's largest institutions. GX F–14 was an exhibit to the Faragher Deposition. Government trial counsel believes that this deposition was offered and admitted but that through error the court reporter failed to record it. We are endeavoring to verify this. The exhibit was subsequently rejected by the court as immaterial to the government's offer to show the price NBC was willing to pay for the acquired bank (Tr. 593).

4. *GX G–5, G–6 and G–10.* They were cited (J.S., p. 17, n. 10) to support the proposition that NBC had negotiated to acquire a smaller bank, the Farmers and Merchants Bank, in the Spokane suburbs. They were rejected (Tr. 606, 610), but this proposition is supported by GX G–2, G–3, G–7, G–8, G–9 and by P.T.O. VIII, Exhs. E and F, pt. IX.

5. The government cited the *Stanton Deposition* (J.S., p. 6, n. 3a) to show that the acquired bank had a potential for expansion in Eastern Washington. According to government trial counsel, this deposition was offered and admitted into evidence, but through a reporter's error is not reflected in the transcript. As with the Faragher Deposition, we are attempting to verify this.

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